PERSPECTIVES

Elect to Leave Your Portfolio Alone

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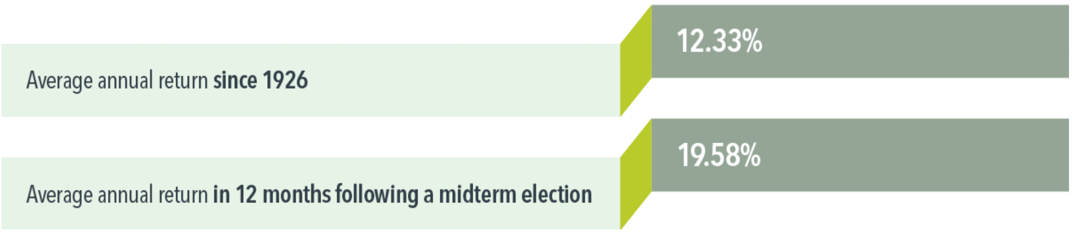
On November 8, US voters will cast their ballots for all 435 seats in the House of Representatives and 35 seats in the Senate. Many investors are concerned with the effect of election results. Do past results suggest a useful strategy to deal with election-year uncertainty?

The answer is yes.

For the 96-year period ending in 2021, the S&P 500 Index (with dividends reinvested) posted an average return of 12.33% for all calendar years and results were negative in roughly one out of four. During that time there were 24 midterm congressional elections. The average return for the 12-month period following the election was significantly higher at 19.58%, with only one negative result.



Average annual return in 12 months following a midterm election begins November in those years. Data source: S&P data © 2022 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved.

Do these numbers suggest investors should load up on stocks just prior to every midterm election? Not so fast. Investors should not make too much of these results—stock returns vary so much from one year to the next that a statistics professor would likely frown on drawing conclusions from only 24 observations. But if investors are looking for reasons to fret over election returns, there is little evidence that changes in political leadership are useful in making portfolio decisions.

These results should come as no surprise. Voters express their opinion at the midterm ballot box once every four years. Consumers express their opinion at the cash register every day by deciding which products and services to buy. Many of us have firmly held opinions regarding politics and policy, but we don't invest in 535 men and women gathering in Washington D.C.

We invest in companies located in Moline, Illinois (Deere & Co.), Los Gatos, California (Netflix), and Bentonville, Arkansas (Walmart). Government policies may have an effect—either positive or negative—on some firms, but the men and women running these firms face challenges and opportunities from dozens of factors. Jim Farley has to juggle resources at Ford Motor to maintain the F-150 pickup truck as the best-selling vehicle in the country while investing in new technology to power models with electric motors. Bob Chapek has to decide how much of Disney shareholders' money should be spent on new cruise ships and how much on movies. Vicki Hollub of Occidental Petroleum must determine if it's best to use healthy cash flow this year to pay down its substantial debt or ramp up exploration efforts.

Are these CEOs concerned with election results? Quite possibly. But we suspect they are far more concerned with a host of issues they face while directing organizations with operations and employees in multiple countries around the world. The same goes for the thousands of other companies, large and small, across the US that are looking for ways to maximize profits for shareholders.

Predicting election outcomes is difficult, and predicting how securities markets will react to those outcomes is harder still.

1986 was a midterm election year. Two prominent retail firms—Walmart and Sears, Roebuck—had a similar market value for their common shares at that time: $13–$15 billion. Walmart continued to prosper and its market value reached $352 billion as of September 30, 2022.[1] Sears shares became worthless following bankruptcy proceedings in 2018. How many of us can recall the most pressing election campaign issues of 1986? And how significant were those political trends more than 30 years ago in explaining why one company survived and the other failed?

Tesla made its initial public offering of shares in 2010 priced at $17. Adjusted for two stock splits, the shares were valued at $3,346 on October 7, 2022.[2] Was Tesla's success a result of generous government tax credits to electric vehicle buyers, or its ability to produce and sell nearly one million vehicles a year despite no previous manufacturing experience? Or some combination of both?

Many investors have firm convictions regarding politics and policy, and a healthy democracy depends on active citizen participation. But predicting election outcomes is difficult, and predicting how securities markets will react to those outcomes is harder still. Did anyone predict that Joe Biden would be elected president and that the US stock market would have its strongest election-week results since 1932?

The takeaway—Dimensional founder David Booth said it best: Vote with your ballot. Not your life savings.

1. Data source: CRSP data is provided by the Center for Research in Security Prices, University of Chicago.
2. Data source: Bloomberg data provided by Bloomberg.

Risks

Investments involve risks. The investment return and principal value of an investment may fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original value. Past performance is not a guarantee of future results. There is no guarantee strategies will be successful.

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